

## Message Text

CONFIDENTIAL

PAGE 01 BRASIL 08159 01 OF 02 261525Z

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ACTION ARA-10

INFO OCT-01 ISO-00 SP-02 AID-05 EB-04 NSC-05 RSC-01

CIEP-01 TRSE-00 SS-15 STR-01 OMB-01 CEA-01 CIAE-00

COME-00 FRB-01 INR-05 NSAE-00 XMB-02 OPIC-03 LAB-01

SIL-01 AGR-05 INT-05 DODE-00 PA-01 USIA-06 PRS-01

PM-03 /081 W

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P R 261455Z OCT 74

FM AMEMBASSY BRASILIA

TO SECSTATE WASHDC PRIORITY 6181

INFO AMCONSUL RIO DE JANEIRO

AMCONSUL SAO PAULO

C O N F I D E N T I A L SECTION 1 OF 2 BRASILIA 8159

E.O.11652: GDS

TAGS: PINT, ECON, EFIN, EGEN, BR

SUBJECT: GOVERNMENT ANNOUNCES EXTRAORDINARY WAGE MEASURE

SUMMARY: PRESIDENT GEISEL ON OCTOBER 24 ANNOUNCED  
LENGTHY PACKAGE OF WAGE, FISCAL AND MONETARY DECISIONS  
THAT REPRESENTED A MAJOR DEPARTURE FROM EXISTING WAGE  
POLICY AND SHOWED NEW ATTENTION TO PROBLEM OF EXPANDING  
DOMESTIC CONSUMPTION. THE MEASURES SEEMED CLEARLY  
DESIGNED TO STILL MOUNTING PUBLIC CONCERN OVER INFLATION  
AND TO CURB THE RECENTLY IMPROVED PROSPECTS OF THE  
OPPOSITION IN THE NOVEMBER 15 ELECTIONS. IT ALSO DISPLAYED  
A REMARKABLE RESPONSIVENESS TO WHAT FINALLY WERE  
SOCIAL PRESSURES. END SUMMARY

1. ON OCTOBER 24, FOLLOWING A MEETING OF HIS FULL  
CABINET OF MINISTERS FROM WHICH AN EXTRAORDINARY  
WAGE MEASURE TO COMPENSATE FOR THIS YEAR'S HIGH  
INFLATION WAS ANTICIPATED, PRESIDENT GEISEL ANNOUNCED  
A LENGTHY PACKAGE OF WAGE, FISCAL AND MONETARY DECISIONS  
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PAGE 02 BRASIL 08159 01 OF 02 261525Z

THAT REPRESENTED A MAJOR DEPARTURE FROM EXISTING WAGE

POLICY AND SHOWED NEW ATTENTION, FORSHADOWED EARLIER IN GEISEL'S 1975-79 NATIONAL DEVELOPMENT PLAN, TO ENCOURAGE THE EXPANSION OF DOMESTIC CONSUMPTION. THE PRINCIPAL MEASURES ANNOUNCED INCLUDE:

--- "EMERGENCY" WAGE ADJUSTMENT OF 10 PERCENT EFFECTIVE DECEMBER 1 FOR ALL WORKERS AT THE MINIMUM SALARY LEVEL AND THOSE WHOSE ANNUAL WAGE ADJUSTMENT TOOK PLACE IN THE FIRST HALF OF THE YEAR. THE PURPOSE OF THIS MEASURE WAS TO COMPENSATE, IN ADVANCE OF THE ANNUAL WAGE ADJUSTMENT IN MAY, FOR A PORTION OF THE DISCREPANCY BETWEEN THE 15 PERCENT INFLATION FIGURE USED FOR THIS YEAR'S WAGE ADJUSTMENT AND THE CURRENT 1974 INFLATION RATE OF 32-34 PERCENT:

--- FEDERAL CIVIL SERVICE AND MILITARY WILL RECEIVE A 30 PERCENT INCREASE, 10 PERCENT EFFECTIVE IN DECEMBER AND THE REMAINDER NEXT MARCH:

--- WITHHELD PERSONAL INCOME TAX WILL BE ENTITLED TO MONETARY CORRECTION WHEN TAX RETURNS ARE DUE:

--- CENTRAL BANK WILL PROVIDE A SPECIAL CRUZEIRO 2 BILLION LINE OF CREDIT TO FINANCE COMPANIES FOR CONSUMER PURCHASES (THIS FOLLOWS A RECENT CR1.3 BILLION SPECIAL INJECTION OF LIQUIDITY THROUGH THE BANK OF BRAZIL):

--- TO CUSHION IMPACT OF WAGE INCREASE, COMPANIES WILL BE GIVEN TAX ADJUSTMENTS ON DISTRIBUTED PROFITS AND A 30 DAY DEFERRAL OF PAYMENTS OF THE INDUSTRIAL PRODUCTS TAX (IPI) ON MOST PRODUCTS: GOVERNMENT WILL ALSO ACCELERATE DISBURSEMENTS OF OBLIGATIONS TO PRIVATE COMPANIES ON REIMBURSABLE SURTAXES AND COMPULSORY LOANS:

--- TAX ON FOREIGN INTEREST PAYMENTS AND OTHER CHARGES ON FOREIGN LOANS WILL BE REDUCED TEMPORARILY (NO PERIOD SPECIFIED) FROM 25 PERCENT TO 5 PERCENT. THIS MEASURE EXCLUDES SHORT TERM LOANS AND IMPORT FINANCING.

2. COMMENT: THE 10 PERCENT "EMERGENCY" WAGE ADJUSTMENT IS THE FIRST MAJOR DEPARTURE IN GOB GENERAL INCOMES POLICY SINCE 1966 WHEN THE ANNUAL ADJUSTMENT FORMULA WAS ADOPTED. FOR SEVERAL WEEKS GOVERNMENT SPOKESMEN HAVE INDICATED THAT THE WAGE ADJUSTMENT IN 1975 WOULD BE 30-35 PERCENT AND THEY EXPLAIN THE ACTION TAKEN THIS WEEK AS AN ADVANCE ADJUSTMENT  
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PAGE 03 BRASIL 08159 01 OF 02 261525Z

TO RELIEVE THE PRESSURES OF INFLATION ON WAGE AND SALARY EARNERS AND TO PROVIDE A STIMULUS TO THE DOMESTIC MARKET. WHETHER THIS WILL BE A ONE-TIME CORRECTION PERMITTING A "NORMAL" 20-25 PERCENT WAGE ADJUSTMENT NEXT YEAR WILL DEPEND ON THE COURSE OF INFLATION OVER THE NEXT SIX MONTHS. THE GOVERNMENT'S BUDGET POSITION THIS YEAR HAS BEEN STRONG AND WILL ALLOW ABSORPTION OF SOME OF THE INFLATIONARY EFFECTS

OF THE NEW MEASURES. THE TAX REDUCTIONS ON FOREIGN BORROWING AIMS TO IMPROVE THE CASH POSITIONS OF COMPANIES AND TO HELP SHORE UP THE BALANCE OF PAYMENTS. ACCELERATED OR LARGER EXCHANGE RATE ADJUSTMENTS WOULD ALSO SEEM A LIKELIHOOD TO CUSHION SOME OF THE IMPACT.

3. WHATEVER ECONOMIC FACE THE GOVERNMENT MAY TRY TO PUT ON THIS MEASURE, IT IS ITS UNMISTAKABLE POLITICAL PURPOSE THAT IS DRAWING THE PRINCIPAL REACTION. OPPOSITION POLITICIANS AROUND THE COUNTRY, WHO HAD PREVIOUSLY BECOME INCREASINGLY CONFIDENT OF A STRONG MDB SHOWING, SAW THEMSELVES BEING DEPRIVED OF THEIR MOST EFFECTIVE ISSUE AND THEY UNDERSTANDABLY SOUGHT TO MINIMIZE THE DAMAGE BY LABELING THE MEASURE BLATANTLY POLITICAL AND AT THE SAME TIME, WITH SOME JUSTIFICATION, TRYING TO CLAIM RESPONSIBILITY FOR IT. (WHILE MDB LEADERS, MOST NOTABLY SENATOR NELSON CARNEIRO, HAD RECENTLY CALLED FOR SUCH A MEASURE, SO HAD ARENA SENATOR FROM SAO PAULO CARVALHO PINTO, WIDELY CONSIDERED TO BE RUNNING BEHIND IN HIS BID FOR RE-ELECTION. THE LATTER'S SUGGESTION WAS ROASTED BY AN UNIDENTIFIED FINANCE MINISTRY "TECHNICIAN" AND FORMALLY REBUFFED OCTOBER 8 IN A FINANCE MINISTRY NOTE REAFFIRMING NO CHANGE IN GOVERNMENT WAGE POLICY. (TWO WEEKS LATER, FINANCE MINISTER SIMONSEN SUDDENLY ANNOUNCED THAT THE SUGGESTION WAS WORTHY OF STUDY AND A PROPOSAL WOULD BE PRESENTED TO THE PRESIDENT.) THE ELECTORAL PURPOSE OF THIS REVERSAL OF LONG-STANDING POLICY IS UNDERSTANDABLE ENOUGH: WHILE IN RECENT MONTHS VARIOUS GOVERNMENT SOURCES HAD PUBLICLY AND PRIVATELY NOTED THE IMPORTANCE TO THE CURRENT POLITICAL SYSTEM OF THE CONTINUED EXISTENCE OF AN OPPOSITION PARTY, IT IS ALSO CLEAR THAT THE REVOLUTION IS PSYCHOLOGICALLY

CONFIDENTIAL

PAGE 04 BRASIL 08159 01 OF 02 261525Z

UNEQUIPPED FOR A REBUFF AT THE POLLS, AND SUCH A RESULT SEEMED TO MANY TO BE IN THE OFFING.

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PAGE 01 BRASIL 08159 02 OF 02 261533Z

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ACTION ARA-10

INFO OCT-01 ISO-00 SP-02 AID-05 EB-04 NSC-05 RSC-01

CIEP-01 TRSE-00 SS-15 STR-01 OMB-01 CEA-01 CIAE-00

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FM AMEMBASSY BRASILIA

TO SECSTATE WASHDC PRIORITY 6182

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C O N F I D E N T I A L SECTION 2 OF 2 BRASILIA 8159

4. WE TAKE THE GOVERNMENT TO HAVE BEEN REACTING NO MORE TO THE ELECTORAL THREAT THAN TO PRESSURES ON OTHER FRONTS: INDICATIONS OF GROWING MALAISE IN THE MILITARY OVER MOUNTING COST-OF-LIVING PROBLEMS; EXPRESSIONS OF CONCERN FROM SECURITY SERVICES OVER GENERAL PUBLIC DISCONTENT OF THE SAME SORT; AND PUBLIC MANIFESTATIONS OF THAT DISCONTENT, MOST DRAMATICALLY IN THE RECENT SPONTANEOUS SACKING OF RAILROAD CARS IN RIO AND STONING OF BUSES IN BRASILIA.

5. ON A BROADER PLANE, THE MEASURE REVERSES NOT ONLY WAGE POLICY BUT THAT MUCH-COMMENTED SITUATION INWHICH THE "SYSTEM" PERMITTED THE COUNTRY'S LEADERS AND TECHNOCRATS TO CARRY OUT THEIR TOUGH, ANTI-INFLATIONARY MEASURES FREE FROM PUBLIC PRESSURES. IN DISTINCT CONTRAST WITH THE PAST, THEN, THE MEASURE SHOWS THE GOVERNMENT RESPONDING TO WHAT IN THE FINAL ANALYSIS ARE SOCIAL PRESSURES. IN THIS SENSE, IT HAS THUS MOVED CLOSER TO THE SITUATION OF GOVERNMENTS IN FAR MORE OPEN SOCIETIES.

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PAGE 02 BRASIL 08159 02 OF 02 261533Z

6. FURTHER ANALYSIS OF THE ECONOMIC AND POLITICAL IMPLICATIONS OF THIS QUITE DRAMATIC DEPARTURE FROM LONG-STANDING POLICY OF THE RVOLUTION WILL FOLLOW.  
END COMMENT:  
CRIMMINS

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